

**TO: THE CHIEF EXECUTIVE OR MANAGING OFFICER AND
CHAIRMAN OF THE AUDIT COMMITTEE OF ALL LOUISIANA
STATE-CHARTERED BANKS AND THRIFTS**

FROM: SID SEYMOUR, CHIEF EXAMINER

DATE: SEPTEMBER 22, 2006

RE: OFI UPDATE

Overall Financial Condition -- Following the one year anniversary of Hurricane Katrina, a vast majority of the banks and thrifts in Louisiana remain in sound financial condition. As of June 30, 2006, there were 166 banks and thrifts domiciled in the state, with 134 or approximately 80% being state-chartered. As of June 30, 2006, 94% of all the banks domiciled in the state had a composite CAMELS rating of 1 or 2. This was unchanged from June 30, 2005. As of June 30, 2006, 89% of all the thrifts domiciled in the state had a composite CAMELS rating of 1 or 2. This was down from 97% as of June 30, 2005. State-chartered banks and thrifts experienced upgrades primarily in the areas of management and earnings, and downgrades in asset quality. During this same period, four new bank charters were issued by this Office. Collectively, these de novo bank groups raised \$105 million in capital. Based on this significant investment, it is clear that these groups share your confidence in the state's economy and commitment to its recovery efforts.

2006 Regular Legislative Session – While no depository-specific legislation was enacted as a result of the 2006 Regular Legislative Session, you may find a complete list of industry-related legislation attached and on our website at www.ofi.louisiana.gov. The short summaries are meant to inform you of the general contents of the legislation and should not be relied upon in lieu of a complete reading of each act. In order to read the Act in its entirety, simply go to our website and click the link “Index of Acts from the 2006 Legislative Session” which is located under “What’s New at OFI.” This link is permanently located under the “Statutes” section of our website. Click on “Statutes” on the left menu bar and then click on the link “Index of Acts from the 2006 Legislative Session.” The enrolled bills can also be found at the Legislature’s website at: www.legis.louisiana.gov. Please contact General Counsel Sue Rouprich at 225/922-1028 or by email at srouprich@ofi.louisiana.gov with any questions regarding this legislation.

Review of the ALLL Account -- On July 2, 2001, an Interagency Policy Statement entitled, “ALLL Methodologies and Documentation for Banks and Savings Associations” was issued. The policy statement requires that financial institutions apply GAAP in establishing a well-documented ALLL. As part of our routine examination procedures, examiners will review methodologies for compliance with the Interagency Policy Statement. We are currently providing additional guidance and training to our examination staff concerning the Allowance for Loan and Lease Losses (ALLL), concentrating on what constitutes adequate methodologies and mitigating factors. If an institution does not correctly apply GAAP, or does not properly document and substantiate the need for its recorded ALLL balance, examiners have been instructed to communicate the need to become compliant with the policy statement. Examiners will also suggest that you meet with your CPAs to establish an ALLL in accordance with the policy statement and GAAP.

We understand and share your desire to maintain a strong ALLL account. We are simply asking that you support the ALLL with documentation that demonstrates that the amount is appropriate. In addition to

historical loss experience, institutions must consider (and document) a number of factors in estimating the amount of probable impairment in their loan portfolios resulting from current events existing prior to the issuance of the financial statements. Factors include, but are not limited to, the following: changes in (1) underwriting standards or lending procedures and policies; (2) charge-off and recovery practices; (3) national and local economic and business conditions; (4) the nature and volume of loans; (5) trends in volumes of past due and classified loans; (6) the quality of an institution's loan review system and degree of oversight by its Board of Directors; (7) the levels and concentrations of loans; and (8) external factors such as competition and legal and regulatory requirements on borrowers. NOTE: GAAP does not allow institutions to increase the ALLL for future events, such as future hurricanes or future crop failures. The ALLL should only provide for estimated losses that have occurred from a current or prior period. Please contact Staff CPA Mrs. Dale Jacobs at 225/922-0632 or by email at djacobs@ofi.louisiana.gov if you have any questions in this regard.

Investment in Bank-Owned Life Insurance (BOLI) -- Examiners continue to check for compliance with the December 7, 2004, BOLI guidance issued by the federal banking agencies. We recognize that some financial institutions may be considering the purchase of separate account BOLI. Please be advised that separate account products, as well as additional riders purchased in connection with these products, expose financial institutions to various risks that must be considered and are covered in several sections of the guidance. It is important that you become familiar with the requirements contained in the guidance before considering the purchase of this product. If you have any questions in this regard, please contact Staff CPA Mrs. Dale Jacobs at 225/922-0632 or by email at djacobs@ofi.louisiana.gov.

Role of Audit Committees – Our examiners have recently received training and will be stressing the important role of audit committees at future examinations. They will meet with audit committees to discuss questions they may have about their duties and responsibilities as well as to review significant examination findings or deficiencies in the internal or external audit process.

As part of this focus, we are continuing our review of internal controls relating to your institution's written policies or written procedures regarding the approval and payment of executive expenses. Following a number of inquiries requesting clarification of the Regulation O implications arising from executives charging personal expenses to corporate credit cards, we held numerous discussions with our federal counterparts. Following these discussions, the Board of Governors of the Federal Reserve System issued new guidance in this regard. A summary of these discussions and the changes that followed are attached in a separate memo.

As a result, OFI is **revising** OFI Bulletin BL-02-2005 dated July 15, 2005, and **rescinding** OFI Bulletin BL-03-2005 dated August 5, 2005. The revised bulletin, OFI Bulletin BL-03-2006 dated September 20, 2006, is attached and has been posted to our web site at www.ofi.louisiana.gov. **I trust that you will agree that the new guidance is more reasonable and less likely to result in apparent violations of Regulation O.** Please contact me at 225/925-4675 or by email at sseymour@ofi.louisiana.gov with any questions.

Mineral Interests -- In a previous update, you were advised that mineral interests acquired in connection with debts previously contracted (DPC) may be held without notification or application to the FDIC as long as the property is being passively held (not for active use) for less than ten years from the date of acquisition. **Please note, however, that the signing of a mineral lease conveying this mineral interest triggers the requirement that you file a notification or application with the FDIC.** Once the ten year divestiture period has transpired, the property, with the mineral interests intact or severed from the property, must be moved to a single purpose subsidiary. Currently, you must file a notification or application with the FDIC to

continue to hold the mineral interests. However, we continue to voice our concerns to the FDIC regarding the treatment of risks associated with the leasing of mineral interests. The FDIC has shared its internal guidance with this Office and several inquiring institutions. It also intends to issue a Financial Institution Letter (FIL) on this topic to its regulated banks. In the meantime, please continue to contact this Office and the FDIC if you have any questions pertaining to the holding of mineral interests.

Residential Mortgage Lending Act -- You are reminded that banks and thrifts, including their direct and indirect subsidiaries, and employees/exclusive agents, are exempt from the licensing provisions of the Louisiana Residential Mortgage Lending Act (RMLA). However, financial institutions, including these other entities, are subject to Part III of the Act which covers certain limits on fees and charges. This part (LSA-R.S. 6:1095-1099) also requires a separate disclosure in instances where loans are brokered under the RMLA. Please note that several important changes were made to the RMLA during the 2006 Regular Legislative Session.

Changes that specifically impact financial institutions include the following: (1) a prohibition on prepayment penalties when prepayment is the result of insurance proceeds received as a result of damage caused by a gubernatorial-declared disaster; and (2) prohibition on including single premium credit life, dismemberment, health and accident, mortgage life and disability, unemployment, collateral protection, or debt cancellation insurance in the loan amounts of any loan subject to the RMLA. Please refer to the websites mentioned previously in order to read the legislation in its entirety.

Direct and indirect subsidiaries of holding companies require licensure and are subject to the RMLA in its entirety. (LSA-R.S. 6:1081-1099). The employees and exclusive agent originators for these subsidiaries remain exempt from the licensure provisions but are subject to the RMLA in its entirety. If you have any questions regarding the RMLA, please contact Deputy Chief Examiner Darin Domingue at 225/922-2596 or by email at ddomingue@ofi.louisiana.gov.

Information on the Conference of State Bank Supervisors' (CSBS) Website – If you haven't checked out the CSBS website lately, it would certainly benefit you to take the time to review it. Their weekly newsletter will update you on the most current matters affecting the state banking system, like Basel II and the commercial real estate proposals, along with current events in each state's and the federal regulatory environment. This direct link to the current newsletter is located at <http://www.csbs.org/Content/NavigationMenu/PublicRelations/CSBSExaminer/ExaminerMain.htm>. Their homepage, <http://www.csbs.org>, has links to the Basel Ia calculator at <http://www.csbs.org/Content/NavigationMenu/Home/BaselIaInfo.htm> in which you may calculate the potential change in minimum capital requirements if the proposed rule were to become final, an Information Security Handbook at <http://www.csbs.org/Content/NavigationMenu/Home/InfoSecHandbookColor.pdf> that will help you comply with the FFIEC's new information security standards, and interactive learning blog/podcasts at <http://innovativelearning.blogs.com/> that give short video clips on some of the hot topics of financial institution regulatory matters such as the home equity lending market, BSA, Basel II, and Sarbanes-Oxley. Please contact Deputy Chief Examiner Kerry Morris at 225/925-4201 or by email at kmorris@ofi.louisiana.gov with questions about CSBS' website or for help accessing the information.

Money Services Businesses (MSBs) -- As a reminder, you are responsible for verifying that a MSB has met state licensing requirements and is registered with FinCEN. You may verify that an MSB is registered with FinCEN by obtaining a copy of the filing directly from the MSB or checking the status online at www.msb.gov. Regarding MSBs, OFI licenses money transmitters and check cashers, but we have different

requirements for licensure than the FinCEN requirements for registering as a MSB. The key requirement for being a MSB is that at least one transaction dealing in the exchange of currency, cashing checks, or issuing, selling, or redeeming traveler's checks, money orders, or stored value exceeds \$1,000. The state licensing requirements for money transmitters and check cashers are discussed below:

- **Money Transmitters** -- In accordance with LSA 6:1033, a license is required for any person engaging in the business of selling or issuing payment instruments, selling or issuing stored value, or receiving money or monetary value for transmission, including electronic transmission. Exemptions from this license are listed in LSA 6:1034 and include federally insured banks, thrifts, and credit unions, agents of a licensee, such as Western Union or American Express, or a governmental agency. A list of licensed money transmitters is maintained on our website at www.ofi.louisiana.gov, which may be accessed by clicking on the "Sale of Checks" key in the left margin, under "DEPOSITORY," then on the "List of Active Sale of Checks Licensees." In a previous update, you were advised that the supervision and regulation of money transmitters was transferred to the depository division. However, the primary contact persons have changed in this area. If you have any questions regarding these licensees, please contact Review Examiner Doug Buras at (225) 922-2595 or by email at dburas@ofi.louisiana.gov or Administrative Specialist Donna Montagnino at (225) 925-4483 or by email at dmontagnino@ofi.louisiana.gov.
- **Check Cashers** – Check cashers are also licensed by this office as required by LSA 6:1003 when a fee of more than \$2.00 is charged to cash a check, draft, money order, or other commercial paper. A list of licensed check cashers is maintained on our website at www.ofi.louisiana.gov, which may be accessed by clicking on the "Check Cashers" key in the left margin, under "NON-DEPOSITORY," then on the "List of Active Check Cashers." If you have any questions regarding these licensees, please contact Administrative Specialist Sandra LeDoux (225) 922-0638 or by email at sledoux@ofi.louisiana.gov.

I want to let everyone know that Deputy Commissioner Doris Gunn's condition has improved, and she continues to undergo treatment for thyroid cancer. For those of you who know Doris, you know that she's strong, both mentally and physically. If you would like to keep up with her progress, her daughter, Kristi, has kept everyone informed of her condition through a blog located at www.doris-report.blogspot.com. You may send messages through this blog, or I will see that she gets any messages or cards if sent to this office.

In closing, I also want to inform everyone that Deputy Chief Examiner Joe Gardner retired effective August 15, 2006, following 27 years of state service. I know you will join with me in wishing him the best in his retirement. I will be happy to forward any messages or cards if sent to this office.

Please do not hesitate to contact me if you have any questions regarding the contents of this update. You may contact me at 225/925-4675 or by email at ss Seymour@ofi.louisiana.gov.